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IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

SEDIMA, S.P.R.L.,

Petitioner,

—v.—

IMREX COMPANY, INC., GIDON ARMON and JACOB ARMON,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

MOTION FOR LEAVE TO FILE A BRIEF AND BRIEF OF THE SECURITIES INDUSTRY ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENTS

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MOTION OF SECURITIES INDUSTRY ASSOCIATION FOR LEAVE TO FILE A BRIEF AS *AMICUS CURIAE*

The Securities Industry Association (the "SIA") respectfully moves, pursuant to Rule 36 of this Court, for leave to file the attached brief as *amicus curiae* in support of respondents. A copy of respondents' consent to SIA's submission of this brief is being filed concurrently herewith. Consent of petitioner, although requested, was not granted.

The SIA is a trade association which represents more than 500 securities firms in the United States and Canada. Its members include investment banks, brokers, dealers and mutual fund companies, as well as other firms functioning on the floors of exchanges. SIA members are active in all exchange and over-the-counter markets and in all phases of corporate and public finance and account for approximately 90% of the securities business in North America.

This case, while not involving claims arising from securities transactions, raises far-reaching questions concerning the proper scope and interpretation of private civil RICO, the resolution of which will have significant impact on participants in the securities markets. With increasing frequency, private civil RICO claims are being included in complaints arising from securities transactions. An interpretation of 18 U.S.C. § 1964(c) consistent with the interpretation of the Second Circuit would accord with the intent of Congress when it enacted RICO and would remove the threat that participants in the securities markets, among others, will be forced to defend inappropriate and abusive litigation.

Members of the SIA, therefore, have a vital interest in this case. In substantial part, this brief will show that the misguided application of private civil RICO threatens to undermine well established statutory and judicial principles applicable to claims involving participants in the securities markets. Because the claims in this case do not arise from securities transactions, it is unlikely that the parties will address this issue in any detail. Moreover, we do not believe that any other *amicus* will focus, to a similar degree, upon the interrelationship between private civil RICO and the federal securities laws.

WHEREFORE, it is respectfully requested that this Court grant the SIA permission to file the attached brief as *amicus curiae*.

Dated: March 29, 1985

Respectfully submitted,

s/ JOEL W. STERNMAN

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BRIEF OF SECURITIES INDUSTRY ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENTS

INTEREST OF *AMICUS CURIAE*

The Securities Industry Association (the "SIA") submits this brief as *amicus curiae* in support of respondents. The SIA urges this Court to adopt an interpretation of private civil RICO[1] consistent with the principles set forth by the United

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1 "RICO", an acronym for "racketeer influenced corrupt organizations," refers to Title IX of the Organized Crime Control Act of 1970, Pub. L. 91-452, 84 Stat. 922, as codified in 18 U.S.C. §§ 1961 *et seq.* "Private civil RICO" refers to 18 U.S.C. § 1964(c), which authorizes civil actions for treble damages at the instance of private parties.

States Court of Appeals for the Second Circuit in *Sedima, S.P.R.L.* v. *Imrex Co.*, 741 F.2d 482 (1984). As relevant here, the statutory language, structure and purpose of 18 U.S.C. § 1964(c) should be held to require private parties to show that defendant was engaged in systematic criminal activity in violation of § 1962 and that, as a result, an injury was sustained which was different in kind from that attributable to the underlying predicate acts. For convenience, this showing shall be referred to as "a distinct RICO injury."

The SIA is a trade association which represents more than 500 firms engaged in virtually all aspects of the securities business. Its membership (which includes investment banks, brokers, dealers, mutual fund companies and specialists) is active in all exchange and over-the-counter markets and in all phases of corporate and public finance. As a group, SIA members account for approximately 90% of the securities business in North America.

The SIA's interest in this case stems from the widespread, and growing, practice of including private civil RICO claims in commercial litigations, such as those arising from securities transactions. As to such transactions, the threat of treble damage liability is both inappropriate and unnecessary when viewed in the context of the existing legislation specifically directed at participants in the securities markets.

The issuance of and trading in securities is one of the most closely scrutinized activities in the American economy. The activities of SIA members are monitored by federal, state and industry enforcement agencies and are subject to regulation under a wide variety of federal and state statutes. The ability of SIA members to do business depends upon the trust of the investing public. That trust is needlessly jeopardized when established institutions are routinely stigmatized as engaging in racketeering.

Because of the impact of private civil RICO on participants in the securities markets, the SIA has a vital interest in *Sedima* as well as in *Haroco, Inc.* v. *American National Bank & Trust Co.*, 747 F.2d 384 (7th Cir. 1984), *cert. granted*, 53 U.S.L.W. 3506 (Jan. 15, 1985) (No. 84-822), even though neither of these cases arises from a securities transaction.[2] As shown below, this Court should adopt a distinct RICO injury requirement consistent with the principles set forth by the Second Circuit in *Sedima* and in *Bankers Trust Co.* v. *Rhoades*, 741 F.2d 511 (2d Cir. 1984), *petition for cert. filed*, 53 U.S.L.W. 3367 (Oct. 24, 1984) (No. 84-657).[3]

SUMMARY OF ARGUMENT

The Second Circuit correctly read § 1964(c) to require private parties to allege a distinct RICO injury in order to state a claim for relief. That injury must be related to systematic criminal activity by defendant in violation of § 1962 and must be different in kind from that attributable to the underlying predicate acts. This requirement, which is consistent with the language and structure of the statute, avoids the displacement of carefully formulated federal legislation such as that regulating participants in the securities markets.

In contrast, the Seventh Circuit's rejection of a distinct RICO injury requirement rests on a misreading of the language of § 1964(c) and a misunderstanding of the role of courts in interpreting a statute in the face of a virtual silence in its

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2 *See Sedima*, 741 F.2d at 496 n.41: "We do not in this business fraud case attempt to define the scope of the standing requirement when the RICO suit is based upon securities law violations."

3 The SIA also believes that, as held by *Sedima*, no private action should be maintainable under § 1964(c) unless the defendants have been criminally convicted. This issue was not addressed in *Bankers Trust*, 741 F.2d at 516 n.5, or in *Alexander Grant & Co.* v. *Tiffany Industries, Inc.*, 742 F.2d 408, 413 n.11 (8th Cir. 1984), *petition for cert. filed*, 53 U.S.L.W. 3541 (Jan. 2, 1985) (No. 84-1084); *see also Haroco* (747 F.2d at 393 n.12), noting that *Sedima*'s criminal conviction requirement conflicts with *Bunker Ramo Corp.* v. *United Business Forms, Inc.*, 713 F.2d 1272, 1286-87 (7th Cir. 1983).

The SIA supports the position respecting the criminal conviction requirement set forth in the *amicus* brief of the American Institute of Certified Public Accountants.

applicable legislative history. In the circumstances presented here, it is the responsibility of the courts to harmonize private civil RICO with the existing legal landscape so as to effectuate Congressional intent. Recognition of a distinct RICO injury requirement would fulfill that responsibility.

ARGUMENT

I

ALLEGATION OF A DISTINCT RICO INJURY IS REQUIRED BY THE LANGUAGE AND PURPOSE OF THE STATUTE

The present controversy arises from a deceptively simple provision authorizing suits by private parties. The private civil RICO provision, set forth in 18 U.S.C. § 1964(c), was added to a statute designed for use by federal law enforcement agencies in fighting organized crime. Section 1964(c) states:

> "Any person injured in his business or property by reason of a violation of section 1962 of this chapter may sue therefor in any appropriate United States district court and shall recover threefold the damages he sustains and the cost of the suit, including a reasonable attorney's fee."

In authorizing claims by private parties, § 1964(c) differs radically from the criminal and public civil provisions of RICO. These are enforceable solely on the initiative of the Department of Justice, which has promulgated a strict set of guidelines governing the commencement of actions by federal authorities.[4] This internal policy-making has obviated the

4 Department of Justice RICO Guidelines, *United States Attorneys' Manual*, Tit. 9, Ch. 110 (adopted Jan. 30, 1981), *reprinted in* 5 Trade Reg. Rep. (CCH) ¶ 50,452. *See Sedima*, 741 F.2d at 497. Among other things, the Guidelines ensure that RICO receives "particularly careful and reasoned application," and that it is not used "far afield from [its] Congressional purpose." The Guidelines also discourage RICO indictments "which merely duplicate the elements of proof of a traditional Hobbs Act, Travel Act, mail fraud [or] wire fraud" case. At the same time, they require centralized authorization from the Department of Justice before a RICO criminal or public civil case can proceed.

danger of inappropriate or overbroad application of the criminal and public civil provisions.

By its terms, § 1964(c) limits the possibility for recovering treble damages to one class of private parties: those "injured . . . by reason of a violation of section 1962." As set forth in *Sedima*, this provision

> "carries with it at least . . . the obligation that the plaintiff show injury different in kind from that occurring as a result of the predicate acts themselves, or not simply caused by the predicate acts, but also caused by an activity which RICO was designed to deter." 741 F.2d at 496.

Thus, a private party must show both that defendant was engaged in systematic criminal activity in violation of § 1962 and that, as a result, an injury different in kind from that attributable to the underlying predicate acts was sustained.

A. Private Parties Must Show That Defendant Violated § 1962 By Engaging In Systematic Criminal Activity

The need for a showing of systematic criminal activity is supported by the articulated purpose for which RICO was enacted and by accepted standards of statutory interpretation.

In the Statement of Findings and Purpose which prefaces the Organized Crime Control Act, Congress made clear that its objective in enacting the statute was the elimination of "organized crime." After an extensive recitation of five findings of fact relating directly to the power and danger of "organized crime," Congress concluded:

> "It is the purpose of this Act to seek the eradication of organized crime in the United States by strengthening the legal tools in the evidence-gathering process, by establish-

ing new penal prohibitions, and by providing enhanced sanctions and new remedies to deal with the unlawful activities of those engaged in organized crime."

This Court has previously indicated "that the legislative history forcefully supports the view that the major purpose of [RICO] is to address the infiltration of legitimate business by organized crime." *United States* v. *Turkette*, 452 U.S. 576, 591 (1981).

The specific goals of Congress in enacting RICO can be effected by the judicial development of standards restricting § 1964(c) to the kinds of systematic criminal activity at which RICO is directed. At a minimum, these standards should require a showing that

1. defendants are associated with a larger criminal organization which has a well-defined hierarchy and structure;

2. to insulate itself from interference, the organization uses violence, intimidation and bribery;

3. the proceeds of its activities are covertly disposed of by illegitimate means or are reinvested in other criminal operations.[5]

The operative criminal sections of RICO do not require that defendants be shown to have an affiliation with organized crime. Apparently this is because some members of Congress were concerned that inclusion of a specific reference to organized crime in the criminal sections might encourage a constitutional challenge on the ground that such a reference would create a so-called status offense. *See, e.g.*, 116 Cong. Rec. 35344 (1970) (remarks of Rep. Poff). However, this

5 *See Moss* v. *Morgan Stanley Inc.*, 553 F. Supp. 1347, 1359-60 (S.D.N.Y. 1983), dismissing a § 1964(c) claim. Although it affirmed that dismissal, the Second Circuit in dictum disagreed with the conclusion of the District Court that a "connection with organized crime" should be viewed as an element of § 1964(c). *Moss* v. *Morgan Stanley Inc.*, 719 F.2d 5, 21 (2d Cir. 1983), *cert. denied*, ___ U.S. ___, 104 S.Ct. 1280 (1984). After *Sedima*, the continued vitality of this dictum, even in the Second Circuit, is doubtful.

concern is irrelevant to the question whether systematic criminal activity should be a prerequisite to claims by private parties under § 1964(c).

A criminal statute will be held to create a status offense only if, without regard to conduct, it subjects an individual to sanctions merely because he joins a particular group or suffers from an undesirable condition. *See, e.g., Robinson* v. *California*, 370 U.S. 660 (1962). However, no status offense is created if, in addition, the statute also requires proof that the individual had a specific intent to further the unlawful purposes of the group or that he failed to submit to appropriate remedial treatment for his condition. Such a statute is constitutional because it punishes conduct, not status. *See Scales* v. *United States*, 367 U.S. 203, 224-28 (1961).

The legislative history of § 1964(c) contains no indication that any member of Congress was concerned over the creation of a status offense in relation to private civil RICO. Indeed, it is undisputed that civil statutes may properly limit liability to members of groups which pursue unlawful goals so long as, in addition, the individual member is shown to have "held a specific intent to further those illegal aims." *NAACP* v. *Claiborne Hardware Co.*, 458 U.S. 886, 920 (1982).

Accordingly, Congressional concern about the creation of a status offense, even if relevant to the interpretation of the criminal provisions of RICO, should not, in any way, affect the propriety of holding that systematic criminal activity is an essential element of a claim under § 1964(c).

B. Private Parties Must Show Injury Different In Kind From, Or Not Simply Caused By, The Underlying Predicate Acts

This component of a distinct RICO injury requirement derives directly from the statutory language. Treble damages can only be recovered upon proof of injury "by reason of a violation of section 1962," the core criminal provision of RICO.

Section 1962 declares unlawful (a) an investment of income derived from a "pattern of racketeering activity" in any enterprise[6] that is engaged in interstate commerce; (b) the acquisition of such an enterprise through a pattern of racketeering activity; (c) the conduct of such an enterprise's affairs through a pattern of racketeering activity; or (d) the conspiracy to do any of the foregoing acts.

"Racketeering activity" is defined as the commission of certain federal or state offenses specified in § 1961(1). These are commonly referred to as "predicate acts." Under § 1961(5) a " 'pattern of racketeering activity' requires at least two acts of racketeering activity" within a ten-year period. The use of the term "requires" rather than "means" in § 1961(5) indicates that proof of two predicate acts constitutes a minimum threshold for RICO liability. Because the statute does not *define* two acts as a "pattern", it leaves the definition for judicial interpretation and development. As one of RICO's principal sponsors explained, "proof of two acts of racketeering activity, without more, does not establish a pattern." 116 Cong. Rec. 18940 (1970) (remarks of Sen. McClellan).

When the relevant statutory provisions are read together, a "violation of § 1962" signifies both a pattern of predicate acts and the use of that pattern to invest in, acquire or conduct the affairs of an enterprise.

Although the aim of the statute is unmistakably at the pattern, not at the individual acts, a pattern in itself does not constitute "a violation of section 1962." A violation occurs only if the pattern is used to invest in, acquire or conduct the affairs of an enterprise. Private parties can therefore recover only if injured as a result of the existence and use of such a pattern. The converse is equally true. Private parties cannot recover if injured only as a result of the underlying predicate acts.

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6 An " 'enterprise' includes any individual, partnership, corporation, association, or other legal entity, and any union or group of individuals associated in fact although not a legal entity." 18 U.S.C. § 1961(4).

Those who favor a broad employment of § 1964(c) challenge requirement of a distinct RICO injury as overly complex. However the sharp distinctions drawn by the statutory language cannot lightly be disregarded. The purpose of § 1964(c) was not to provide enhanced penalties of a civil nature for a random list of criminal acts which were already proscribed. Rather, as recognized by the Second Circuit in *Sedima* and *Bankers Trust* and by the Eighth Circuit in *Alexander Grant*,[7] § 1964(c) was enacted to provide a remedy only for those who had suffered a distinct RICO injury.

II

A DISTINCT RICO INJURY REQUIREMENT HARMONIZES § 1964(c) WITH EXISTING LAW

As shown above, the requirement of a distinct RICO injury is supported by the statutory language and structure. However, because the language of a statute is only the starting point for determining its scope, expressions of Congressional intent, as recorded in the legislative history, usually are consulted next. But the history of § 1964(c) fails to provide any relevant guidance: the simple fact is that Congress devoted almost no attention to private civil claims when it considered RICO.

In the face of the "clanging silence of the legislative history" of § 1964(c) (*Sedima*, 741 F.2d at 492), courts must turn to well established principles to define the scope of this provision in a manner consistent with other applicable law. The strictest attention to this judicial imperative is mandated because § 1964(c) might otherwise be read to infringe on areas already subject to pervasive federal regulation and because its unbridled application threatens to undermine the principle of limited federal jurisdiction.

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7 The Eighth Circuit viewed its decision as consistent with *Bankers Trust* even though it noted that *Bankers Trust* established a higher standard of pleading. It did, however, state that *Sedima*'s injury requirement was contrary to its earlier holding in *Bennett* v. *Berg*, 685 F.2d 1053 (8th Cir. 1982), *on reh.*, 710 F.2d 1361 (*en banc*), *cert. denied*, ___ U.S. ___, 104 S.Ct. 527 (1983).

A. The Legislative History Is Silent On The Scope Of § 1964(c)

In commenting upon the legislative history of private civil RICO, *Sedima* (741 F.2d at 492) stated:

> "The most important and evident conclusion to be drawn from the legislative history is that the Congress was not aware of the possible implications of section 1964(c). If Congress had intended to provide a federal forum for plaintiffs for so many common law wrongs, it would at least have *discussed* it. If Congress had intended to provide an alternate and more attractive scheme for private parties to remedy violations of the securities laws—involving decades of statutes, regulations, commentaries, and jurisprudence—it would at least have *mentioned* it. The House Judiciary Committee, which authored the provision, would at least have mentioned the amendment to the full House as a major change in its report had there been any inkling of its possible implications."

See also Haroco, 747 F.2d at 390, 393:

> "It is true that the legislative history includes relatively little material on RICO's private civil remedy.
>
> * * *
>
> [*Sedima's*] review of the history shows convincingly that the private civil RICO provisions of section 1964(c) received relatively little attention from Congress in the enactment of the omnibus Organized Crime Control Act. The issue is what conclusions should be drawn from that fact."

A private damages provision was not part of the bill originally passed by the Senate. It was added in the House Judiciary Committee, which offered only the following explanation when the amended bill was brought to the House floor:

> "Title IX is designed to inhibit the infiltration of legitimate business by organized crime. In addition to creating new Federal offenses punishable by traditional criminal sanctions . . ., title IX also creates civil remedies modeled on those found in the antitrust field. These include orders of divestment, prohibition against business activity and orders of dissolution or reorganization, and treble damage suits on the part of private parties who are injured." 116 Cong. Rec. 35196 (1970) (remarks of Rep. Celler).

The amended bill was subsequently adopted by the Senate without any discussion.

Because of the total absence of an affirmative statement that private civil RICO relief should be broadly available, those who favor an expansive interpretation argue that Congress' *inaction* after hearing a critic's objection should be viewed as indicating a positive adoption of the objectionable interpretation. Thus, petitioner in *Sedima* (Br. at 39-40) quotes a statement by three opponents of § 1964(c) claiming that the section provided an " 'invitation for disgruntled and malicious competitors to harass innocent businessmen engaged in interstate commerce.' " Petitioner suggests that, by subsequently adopting the statute, Congress intended to leave private civil RICO without any limitations. However, the fears and doubts of the opponents of legislation have repeatedly been rejected as an authoritative guide to its construction. *Selective Service System* v. *Minnesota Public Interest Research Group*, ___ U.S. ___, 104 S.Ct. 3348 (1984); *Schwegmann Brothers* v. *Calvert Distillers Corp.*, 341 U.S. 384, 394 (1951); *see also Sedima*, 741 F.2d at 490 n.22.[8]

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8 There is further reason to conclude that Congress did not intend the massive growth of civil litigation in the federal courts which has resulted from an expansive reading of § 1964(c). A few months before the enactment of RICO, a bill was passed that created 58 new federal district judgeships. As the House Report to Senate Bill 952 (Pub. L. 91-272, codified in 28 U.S.C. § 133) makes plain, Congress was fully aware in 1970 of "the delay and confusion" in the district courts. The House Report noted with concern the "record backlogs" caused by the

B. The Development Of Standards For Private Civil RICO Is An Appropriate Responsibility Of The Courts

Congress failed to supply explicit standards for applying § 1964(c). This fact does not, as the Seventh Circuit apparently believed, support the conclusion that Congress intended that there be no standards at all. Rather, in such circumstances, courts traditionally act to limit the scope of statutes to the objectives Congress clearly identified and expressly sought to achieve. Thus, under the federal antitrust laws, judicially developed standing requirements limit relief only to injuries which flow "from that which makes defendants' acts unlawful." *Brunswick Corp.* v. *Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 489 (1977). In other words, there must be a causal connection between the antitrust violation and the harm suffered. *See, e.g., Associated General Contractors, Inc.* v. *California State Council of Carpenters*, 459 U.S. 519 (1983).

When the alleged injury results solely from a tort or a breach of contract, no antitrust claim is stated. Thus, in *A.D.M. Corp.* v. *Sigma Instruments, Inc.*, 628 F.2d 753, 754 (lst Cir. 1980), " 'mere' unfair business practices or business torts," such as disloyal acts by corporate officials, did not state an antitrust claim. Similarly, in *Chrysler Corp.* v. *Fedders Corp.*, 643 F.2d 1229 (6th Cir.), *cert. denied*, 454 U.S. 893 (1981), a breach of contract claim, allegedly related to anti-competitive activities, lacked an "essential connection" with the antitrust laws because the contract itself was not violative of those laws. *See also Fields Productions, Inc.* v. *United Artists Corp.*, 432 F.2d 1010 (2d Cir. 1970) (*per curiam*), *aff'g* 318 F. Supp. 87 (S.D.N.Y. 1969), *cert. denied*, 401 U.S. 949 (1971), rejecting a claim because the cause of plaintiff's injury was not an antitrust violation—blockbooking of motion pictures—but was an improper allocation of profits.

"sharp" increase from the preceding year of both civil and criminal filings. 1970 U.S. Code Cong. & Ad. News 3221, 3224.

It cannot be assumed that Congress, at the same time it was actively seeking to solve the problem of severely overcrowded dockets, would, without comment or explanation, enact legislation dramatically expanding the *civil* jurisdiction of the federal courts to encompass cases normally—and competently—handled by other courts.

This analytical process should be used to identify claims not properly within the scope of § 1964(c), such as those resting on nothing more than alleged acts of mail fraud or wire fraud and lacking any relationship to the wrongful conduct which Congress explicitly stated it was remedying. The use of this process cannot be assailed on the ground that Congress declined to place RICO, which was designed to ruin racketeer-controlled enterprises,[9] in the antitrust laws, which were designed to enhance competition and to protect "economic freedom." *Associated General Contractors, supra*, 459 U.S. at 538.[10]

C. Well Established Principles Support A Narrow Interpretation Of § 1964(c)

When a broad reading of a statute would lead to unanticipated results, legislative intent has been determined "not by the letter of the law" but by its "spirit." Such a determination takes into account not only the presence or absence of relevant legislative history but also the historical matrix from which the

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9 *See Furman* v. *Cirrito*, 741 F.2d 524, 532 (2d Cir. 1984), *petition for cert. filed*, 53 U.S.L.W. 3343 (Oct. 15, 1984) (No. 84-604). *See also Russello* v. *United States*, 464 U.S. 16, 104 S.Ct. 296, 303 (1983) (RICO was enacted "to remove the profit from organized crime by separating the racketeer from his dishonest gain.").

Some have argued that a distinct RICO injury requirement would inhibit the ability of the public to recoup damages from seriously corrupt entrepreneurs. But efforts to eliminate systematic corruption will not be impeded if private civil RICO is applied in the manner suggested in this brief. Wrongdoers may, as always, still be pursued under other applicable statutes. In any event, the asserted needs of public attorneys do not justify an overbroad reading of RICO in a way that would improperly affect the rights of private parties.

10 As stated by *Sedima*, 741 F.2d at 495:

> "On the other hand, there is nothing in the legislative history which suggests that Congress did not intend to create *analogous* standing barriers to RICO by using the 'by reason of' language. By borrowing language imposing a standing limitation, it is reasonable to believe that Congress indicated a desire to have an analogous standing limitation imposed in RICO."

statute arose and the evil it was designed to remedy. *United Steelworkers* v. *Weber*, 443 U.S. 193, 201 (1979); *Church of the Holy Trinity* v. *United States*, 143 U.S. 457, 459 (1892); *see also Sedima*, 741 F.2d at 488 n.17. A particular sensitivity to context, both historical and statutory, is shown when the broad application of a general statute would disrupt an established regulatory scheme or disturb the traditional allocation of state and federal jurisdiction.

A decision to read a statute narrowly must be made when, as here, a broad reading would be inconsistent with other—and more specifically drawn—statutes. Thus, when one statute thoroughly regulates a particular field, and a broader statute regulates a more general field—arguably including the particular one—the particular field is properly held beyond the reach of the broader statute, absent expressions of Congressional intent to the contrary. *See Radzanower* v. *Touche Ross & Co.*, 426 U.S. 148, 153 (1976) (broad venue provisions inapplicable in actions against national banks): "It is a basic principle of statutory construction that a statute dealing with a narrow, precise, and specific subject is not submerged by a later enacted statute covering a more generalized spectrum."[11]

For similar reasons, *Train* v. *Colorado Public Interest Research Group*, 426 U.S. 1, 23-24 (1976), held that nuclear materials were not subject to regulation by the Federal Water Pollution Control Act (the "FWPCA"), even though, on its face, FWPCA appeared to encompass such materials. Pointing to the pervasive regulation of nuclear materials by the Atomic

11 *Cf. United States* v. *United Continental Tuna Corp.*, 425 U.S. 164, 169 (1976), where it was held that an amendment to the Suits in Admiralty Act did not authorize the bringing of claims which were otherwise barred by the Public Vessels Act. In the absence of "some expression by Congress that such results are intended," this Court declined to find a legislative decision to "compromise or abandon[ ] . . . previously articulated policies."

In such circumstances, the silence of the legislative history "is most eloquent, for such reticence while contemplating an important and controversial change in existing law is unlikely." *Edmonds* v. *Compagnie Generale Transatlantique*, 443 U.S. 256, 266-67 (1979). *See also Sedima*, 741 F.2d at 503-04.

Energy Act, this Court found the legislative history of FWPCA did not contain "the clear indication of legislative intent that we might expect before recognizing such a change in policy."

This narrowing of a statute's scope operates forcefully when private rights are fully protected by an existing statute. Thus, in *International Brotherhood of Teamsters* v. *Daniel*, 439 U.S. 551 (1979), the federal securities laws were held inapplicable to pension plans which were regulated by the more precisely drawn ERISA statute. It was noted that, unlike "the Securities Acts, ERISA deals expressly and in detail with pension plans" and that, in light of the "existence of this comprehensive legislation" it would "serve[ ] no general purpose" to apply the securities laws to pension plans. 439 U.S. at 569-70.

See also Marine Bank v. *Weaver*, 455 U.S. 551, 556-59 (1982), where certificates of deposit were found not to qualify as "securities" within the meaning of the Securities Exchange Act of 1934 because the purchasers of these certificates were "abundantly protected" by the federal banking laws.

Courts are also obligated to read a federal statute narrowly when a broad reading would expand federal jurisdiction in ways not intended by Congress. As stated in *Apex Hosiery Co.* v. *Leader*, 310 U.S. 469, 513 (1940):

> "The maintenance in our federal system of a proper distribution between state and national governments of police authority and of remedies private and public for public wrongs is of far-reaching importance. An intention to disturb the balance is not lightly to be imputed to Congress."

See also Santa Fe Industries, Inc. v. *Green*, 430 U.S. 462, 479 (1977), holding certain causes of action beyond the scope of the federal securities laws, and recognizing that "absent a clear indication of congressional intent," it would be inappropriate "to federalize [a] substantial portion of the law of corporations." *Accord: Cort* v. *Ash*, 422 U.S. 66, 84 (1975).

As explained in *Federal Trade Commission* v. *Bunte Brothers, Inc.*, 312 U.S. 349, 351 (1941), "in ascertaining the scope of congressional legislation a due regard for a proper adjustment of the local and national interests in our federal scheme must always be in the background."[12] *See also Sorrells* v. *United States*, 287 U.S. 435, 450 (1932):

> "To construe statutes so as to avoid absurd or glaringly unjust results, foreign to the legislative purpose, is, as we have seen, a traditional and appropriate function of the courts. . . . The Congress by legislation can always, if it desires, alter the effect of judicial construction of statutes."[13]

Thus, the Second Circuit was properly sensitive to its obligation to interpret § 1964(c) by looking to the policy of RICO as a whole and avoiding disruption of well established rules of law.

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12 Proponents of broad application of private civil RICO mistakenly rely upon *United States* v. *Turkette*, *supra*, for the proposition that Congress intended to federalize large bodies of state common law when it enacted RICO. A fair reading of *Turkette* shows that it considered only the Congressional intent to "alter somewhat the role of the Federal Government in the war against organized crime." 452 U.S. at 587. *Turkette* did not consider the purpose of private civil RICO.

13 In October 1984, the Chairman of the Senate Judiciary Committee stated:

> "[T]he civil RICO part of title IX [of the Organized Crime Control Act of 1970] was crafted to enhance the protection of legitimate businesses against the syndicate's infiltration by dealing with the organized crime as an economic phenomenon.
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> • • •
>
> [W]hen we acted on this RICO statute as part of the Organized Crime Control Act of 1970, I think it is fair to observe that we might not have envisioned the full use of the statute by private civil litigants to include a civil RICO count in their ordinary business litigation alleging misstatements and fraud." 130 Cong. Rec. 13349-50 (remarks of Sen. Thurmond).

Subsequently, Senator Thurmond commented that RICO had "been perverted by fertile legal minds" and was disrupting the traditional allocation of jurisdiction between the federal and state courts. Daily Report for Executives (BNA), at A-2 (Jan. 9, 1985). *See also* Task Group on Regulation of Financial Services, *Blueprint For Reform* (1984). As relevant here, this report, which was publicly released by Vice President Bush in November 1984, stated (p. 96) that there had been a "flagrant misuse of RICO as a tool of strike [suit] litigation against financial firms with no connection whatsoever to the organized crime activity RICO was designed to deter."

In contrast, the approach of the Seventh Circuit ignores the fact that, without a judicial delineation of appropriate boundaries, the circumstances in which private civil RICO may be applied are limitless. Even though that Court recognized that it did "not seem at all likely that Congress anticipated" RICO would apply to interest rate overcharges, it mistakenly believed that it would constitute "aggressive jurisprudence" to channel the statute in the direction Congress intended. *Haroco* at 392, 399; *see also Sutliff, Inc.* v. *Donovan Cos.*, 727 F.2d 648, 654 (7th Cir. 1984); and *Schacht* v. *Brown*, 711 F.2d 1343, 1361 (7th Cir.), *cert. denied*, ___ U.S. ___, 104 S.Ct. 509 (1983). This approach may not, in the circumstances, be viewed as an appropriate exercise of deference to legislative judgment because it fails to recognize the significance of the fact that Congress did not anticipate the application of private civil RICO in the manner in which it is being used.

The recognition of a distinct RICO injury requirement for § 1964(c) would therefore be in accord not only with Congress' intent as to criminal and public civil RICO but also with accepted canons of statutory interpretation.[14]

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14 Proponents of an unlimited reach for private civil RICO rely heavily on § 904 of the Organized Crime Control Act, which provides that it "shall be liberally construed to effectuate its remedial purposes." However, that provision cannot be used to distort the statute or to absolve the courts of their obligation to look at "Congress' intent when it passed the legislation" instead of making "unverifiable guesses as to what its intent would be" in procedural and factual contexts which were not contemplated. *Aetna Casualty and Surety Co.* v. *Liebowitz*, 730 F.2d 905, 908-09 (2d Cir. 1984).

III

MISGUIDED APPLICATION OF PRIVATE CIVIL RICO WOULD UNDERMINE STATUTORY AND JUDICIAL PRINCIPLES APPLICABLE TO CLAIMS INVOLVING PARTICIPANTS IN THE SECURITIES MARKETS

The compelling need for a distinct RICO injury requirement is demonstrated with particular force when claims under § 1964(c) are asserted in areas pervasively regulated by federal statutes. Adjudication of such claims could substantially disrupt the functioning of statutes applicable to creditors' rights, pension benefits, and banking, commodities and securities transactions. This problem will be illustrated by reference to the potential effects of private civil RICO on securities litigation.[15]

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15 Two RICO provisions—§§ 1961(1)(D) and 1962(a)—make specific references to securities. Neither contains any indication that Congress intended that RICO displace the federal securities laws.

Section 1961(1)(D) includes "fraud in the sale of securities" in the list of predicate offenses. This provision was added in the Senate only because of a concern that members of organized crime were infiltrating the securities markets and creating a danger of organized theft or counterfeiting of securities, use of stolen securities as collateral for bank loans and manipulation of large blocks by criminal elements. *Measures Relating to Organized Crime: Hearings Before the Subcomm. on Criminal Laws and Procedures of the Senate Comm. on the Judiciary*, 91st Cong., 1st Sess. 154, 227 (1969); *see also Organized Crime Control: Hearings on S.30, and Related Proposals Before Subcomm. No. 5 of the House Comm. on the Judiciary*, 91st Cong., 2d Sess. 106 (1970); McClellan, *The Organized Crime Act (S. 30) or Its Critics: Which Threatens Civil Liberties?*, 46 Notre Dame Law. 55, 143 (1970) (quoting testimony of J. Edgar Hoover).

Section 1962(a), which declares unlawful the use of funds derived from a pattern of racketeering activity "in acquisition of any interest in, or the establishment or operation" of certain enterprises, is, by its terms, inapplicable to a "purchase of securities on the open market for purposes of investment, and without the intention of controlling or participating in the control of the issuer," unless more than 1% of the outstanding securities are acquired. This "1% exception" was added at the suggestion of the Department of Justice. The reference to securities in defining activities beyond the scope of RICO obviously cannot support a broad application of § 1964(c) to securities transactions.

Participants in the securities markets are subject to numerous tiers of regulatory authority. At the apex is the Securities and Exchange Commission, whose enforcement arm has powers to seek injunctive relief, as well as criminal and civil penalties. Participants are also policed administratively by the various securities exchanges, by the National Association of Securities Dealers, and by regulatory authorities in virtually every state. In addition, they are subject to civil suit for violations of federal and state securities laws as well as for claims based upon common-law principles.

For more than fifty years, courts have paid meticulous attention to the operative provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934, as well as other applicable statutes, and have formulated a comprehensive body of law regarding the elements of private claims for relief. Careful scrutiny has been paid to such matters as standing, culpability, causation, reliance and materiality, as well as to the definitions of "securities" and of "fraud".

Furthermore, courts have devoted substantial attention to the interrelationship of the various statutory and regulatory provisions and to the question whether a particular provision can be enforced by private parties. The issues determined have required, among other things, attention to the specific language of the statute, to Congress' intent in enacting it and to the public purpose which it serves.

As indicated by the following decisions, issued since *Sedima* was decided, private parties are including claims under § 1964(c) in complaints which already contain—or could contain—claims under the federal securities laws:

(i) churning [*Aliberti* v. *E.F. Hutton & Co.*, 591 F. Supp. 632 (D. Mass. 1984) (motion to add RICO claim denied; civil remedies available under the securities laws); *Grey* v. *Gruntal & Co.*, 84 Civ. 5036 (S.D.N.Y. Dec. 14, 1984) (RICO claim dismissed because no criminal conviction, as required by *Sedima*, and no allegation of distinct RICO injury); *Lopez* v. *Dean Witter Reynolds, Inc.*, 591 F. Supp. 581 (N.D. Cal. 1984)

(leave to amend granted, but no RICO standing if injury only from predicate acts and unless brokerage house organized solely for criminal purposes); *Perritt* v. *Merrill Lynch, Pierce, Fenner & Smith*, 83 C 8557 (N.D. Ill. Jan. 9, 1985) (refusal to dismiss RICO claim, relying on *Haroco*)];

(ii) insider trading [*O'Connor & Associates* v. *Dean Witter Reynolds, Inc.*, 600 F. Supp. 702 (S.D.N.Y. 1985) (RICO claim dismissed, relying on *Sedima* and *Bankers Trust*)];

(iii) sale of worthless bonds or notes [*Sheftelman* v. *Jones*, [Current] Fed. Sec. L. Rep. (CCH) ¶ 91,928 (N.D. Ga. Dec. 26, 1984) (RICO claim dismissed for "failure to make clear the criminal nature of the acts alleged"); *Taylor* v. *Bilezikian*, 84-883 Civ-T-10 (M.D. Fla. Dec. 11, 1984) (RICO claim dismissed, relying on *Sedima*); *Banowitz* v. *State Exchange Bank*, 600 F. Supp. 1466 (N.D. Ill. 1985) (refusal to dismiss RICO claim, relying on *Haroco*)];

(iv) embezzlement from customer accounts (*Bennett* v. *E.F. Hutton Co.*, C83-1502A (N.D. Ohio Nov. 28, 1984) (RICO claim dismissed for pleading insufficiency)];

(v) market manipulation [*Rooney Pace, Inc.* v. *Reid*, 84 Civ. 0471 (S.D.N.Y. Mar. 22, 1985) (RICO claim dismissed, relying on *Sedima*); *Atlantic Federal Savings & Loan Ass'n* v. *Dade Savings & Loan Ass'n*, 592 F. Supp. 1089 (S.D. Fla. 1984) (RICO claim dismissed, relying on *Sedima*)].

Nothing in these decisions indicates that plaintiffs had made allegations of systematic criminal activity or of injury different in kind from that arising from the underlying predicate acts. Rather, they join RICO claims to traditional securities claims in the hope of obtaining greater damages and attorneys' fees.

The impropriety of allowing RICO claims in securities litigation without allegations of a distinct RICO injury may be illustrated by two examples:

1. A well recognized prerequisite to standing under section 10(b) of the Securities Exchange Act of 1934 is an allegation of

fraud in connection with the purchase or sale of a security. The recognition of this prerequisite is grounded both in statutory language and in policy concepts. Under the view of private civil RICO accepted by the Seventh Circuit, shareholders could assert claims in factual situations barred by *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723 (1975). For example, a customer who refrained from selling a security during a period when its market price was declining could allege that, on two occasions, his broker recommended by telephone that the security not be sold. Similar claims could be asserted by shareholders alleging that, in reliance on statements sent by the issuer through the mails, they refrained from selling the issuer's shares during a period when its market price was declining.[16]

2. Pursuant to 15 U.S.C. § 78bb(a), recovery by private parties under the Securities Exchange Act of 1934 is limited to actual damages. But, by the addition of a RICO claim, a plaintiff could, by that device alone, seek to recover potential treble damages as well as attorneys' fees. Furthermore, if the complaint were certified for class action status, the possible economic consequences could be so ruinous that a defendant might "find it economically prudent to settle and to abandon a meritorious defense." *Coopers & Lybrand* v. *Livesay*, 437 U.S. 463, 476 (1978).

As shown above, Congress gave no indication that it intended to authorize the disruptions which would stem from an expansive application of private civil RICO to all participants in the securities markets. While the punitive purpose of RICO might well justify some of these anomalies in appropriate cases, there is no basis in logic, policy or the legislative record for allowing § 1964(c) to support claims arising from securities transactions in the absence of a distinct RICO injury.

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16 And, as noted in *Sedima*, 741 F.2d at 499, "two misstatements in a proxy solicitation could subject any director in any national corporation to 'racketeering' charges and the threat of treble damages and attorneys' fees."

Recognition that such an injury is required would not constitute "aggressive jurisprudence." Rather, as *Sedima* correctly acknowledged (741 F.2d at 503-04), courts should not

> "impute to Congress the intention of . . . altogether replacing or eliminating much of the need for extensive bodies of federal law specifically directed at extensively considered evils, [without] explicit language from Congress indicative of such intent."

Because they fail to allege a distinct RICO injury, the *Sedima* and *Haroco* claims should be viewed as beyond the scope of § 1964(c). But in the event this Court holds that these particular plaintiffs have succeeded in stating private civil RICO claims it should carefully limit its holding so that § 1964(c) is not rendered applicable to claims otherwise subject to adjudication under pervasive federal legislation such as the securities laws. A limitation of that nature would ensure that well recognized federal statutory principles are not disturbed in the absence of a clear direction from Congress.

CONCLUSION

For the foregoing reasons, the decision of the Second Circuit should be affirmed.

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Respectfully submitted,

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